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Realty Stock Review

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MARKET STRATEGY: LOOK AT 1985'S LOSERS FOR SOME INTERESTING NEW YEAR'S PICKS

Everyone likes to talk about last year's winners at this time of the year, especially since 1985 went into the books with the Dow-Jones Industrials and S&P 500 Index near all-time highs, up 27.8% and 26.3% respectively.

Overall, realty stocks trailed the broad averages by a good margin, reflecting media handwringing about overbuilt and overfinanced properties. Losers were concentrated in the REITs (we include price change from offer price for new issues in making this count) but winners still outnumbered losers, 135 to 76, as follows:

	Winners	Losers
REITs.....	48	42
Operating cos...	87	34

Group performance was pretty much in line with our Dec. 20 issue: Diversified realty and holding company stocks were best performers, followed by the smaller builder/developers, mortgage finance, and realty syndication and service companies. Liquidating companies and combination property/mortgage REITs were the big losers. Here's a tally of biggest percentage gainers and losers, again including price change from offer price for 1985 new issues:

BIGGEST REALTY STOCK GAINERS IN 1985

REITS		OPERATING COMPANIES	
1.Bradley RE..	+119.6	LoanAmer.Fi.	+150.1
2.Pres. Rl.A..	+ 54.5	Amrep Corp..	+112.6
3.Pres. Rl.B..	+ 42.3	Wash. Homes.	+107.2
4.Inv.GNMA....	+ 38.1	Rockwood Na.	+100.3
5.Hotel Prop..	+ 36.3	Nat. Homes..	+100.1
6.Gould Inv...	+ 36.2	Centenn.Grp.	+ 99.5
7.Res.Pens.I..	+ 33.6	Std. Pacif..	+ 99.0
8.Utd.Domin...	+ 30.5	UDC-Univer..	+ 97.1
9.Wedgestone..	+ 28.9	Disney Prod.	+ 88.6
10.Penn.REIT..	+ 27.0	So.Atl.Fin..	+ 87.0

BIGGEST REALTY STOCK LOSERS IN 1985

1.Americana Ho.	-60.3	First City...	-58.2
2.ConCap Specl.	-50.4	Covington Te.	-44.4
3.ConCap Incm..	-41.0	River Oaks...	-43.7
4.Natl.Cap.RE..	-35.0	Fraser Rlty..	-42.3
5.Wespac Inves.	-33.3	Sunstates Cp.	-38.8
6.First Contl..	-29.4	Champion HB..	-38.4
7.ICM Prop.Inv.	-26.2	Zimmer Corp..	-33.3
8.ConCap Rlty..	-25.7	Southland Fi.	-32.8
9.ConCap InOpp.	-25.0	Pulte Home...	-25.6
10.Grubb REIT..	-22.5	Amer.Century.	-24.0

Inside we review some of 1985's biggest losers because our experience shows that last year's laggards very often turn into the leaders for the new year. And last year's big winners seldom repeat. There's a solid reason: investors constantly take profits in big winners and reinvest in lower priced stocks with good potential. This circular money flow is key in your strategy.

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NOW AVAILABLE: Our new brochure describing our money management services and two new separate accounts (TARESA Accounts - The Audit Real Estate Securities Accounts).

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RANKING REVIEW: JOHNSTOWN AMERICAN KEEPS RANK, CONSOLIDATED CAPITAL REALTY FALLS

Johnstown American Cos. holds B Rank in its first review since acquiring the major West Coast syndicator, Consolidated Capital Equities Corp. last July. JAC was one of 1985's bigger losers, falling 19.7% and touching 5 at one point, mainly because ConCap began reporting EPS problems almost immediately after the acquisition. Atlanta based JAC has now recovered to 7 (ASE).

EPS/Dividends - B: JAC earned 69¢ sh. (66¢ diluted) in its Aug. 1985 year, up 11%. But that was a disappointment from expectations in the 80-85¢ range because the Aug. qtr. (first including ConCap) fell to 11¢, off 35%. The Nov. qtr. continued these adverse comparisons as EPS sank to 4¢ (3¢ diluted), down 75%. The EPS outlook for 1986 and beyond now hinges upon JAC's success in two areas, its established property management and advisory operations and its new syndicator/REIT management business. JAC started as a manager of ConCap properties, so the ConCap acquisition eliminates many inherent conflicts. Most JAC business lines are categorized by underlying property ownership, categories being (a) properties owned by ConCap syndication programs; (b) owned by partnerships and entities controlled by JAC or ConCap officers or affiliates; and (c) owned by unrelated parties.

Property management fees jumped 80% to $22.1 mil. in 1985, mainly on a 57% rise in condos and apartment units under management to 165,000 and a 48% jump in commercial space managed to 8 mil. sq. ft. Acquisition of condo association management companies added 32,000 DU, and takeover of management from a West Coast syndicator added 13,000 DU. Units managed for unrelated parties rose to 48% of this total, vs. 33%; the remainder are managed for ConCap programs or private partnerships controlled by officers or affiliates of JAC or ConCap. Advisory fees for construction supervision, security, administration and other consulting services rose 66% to $11.2 mil. with services to unrelated parties being 12% of the total, up from 5%.

Property brokerage and leasing commissions rose 238% to $32.8 mil., the fastest growing segment inside JAC, reflecting acquisition of ConCap (which receives fees for transactions on program properties), and acquisitions of Business Properties Brokerage and Daum Corp. in 1984 and 1985, plus formation of Commercial Real Estate Services subsidiary. About 47% ($15.5 mil.) of revenues are paid as commissions to brokers.

Other revenues include $10.2 mil. carpet sales, about 65% to unrelated parties; $4.1 mil. underwriting commissions on syndication programs (normally almost all re-allowed to participating brokers); $4.6 mil. interest; $3.1 mil gain on collection or sale of properties (mainly from the former Hamilton Investment Trust) and acquired taxloss benefits. A potentially big item, mortgage placement fees from ConCap mortgage programs (see below) was only $0.7 mil. for 6 wks. ConCap was included in 1985.

Outlook: Fiscal 1986 EPS will depend almost entirely upon how fast ConCap turns around, since basic property management and brokerage operations were strongly positive in the Nov. qtr. ConCap earned $2.3 mil. pretax in the Nov. qtr. but $3 mil. interest and amortization brought an overall loss. JAC has trimmed about $6 mil. from ConCap overhead by reducing staff about 16% and cutting executive salaries; most cuts didn't come until near qtr. end, so benefits will surface later this year. ConCap operations were strong as it closed $97 mil. property sales and $79 mil. acquisitions in the Nov. qtr. (on which ConCap earns fees). Mortgage placement fees remained low. Early-on JAC was expecting 80¢-plus for 1986 but this would take a super-strong second half. Equaling 1985 EPS would be an achievement, in our view.

Financial Measures - B: Debt of $98.1 mil. is 1.6 times shareholders' equity of $60.2 mil., which includes $27.5 mil. preferred issued in the ConCap acquisition. Net common equity is $32.66 mil. or $2.76/sh. on 11.6 mil. combined Class A and B shs. Class B shs. were created during the year and have 10 votes per sh. and a lower dividend; they are owned by John Lie-Nielsen, JAC chairman. JAC paid $102.5 mil. for ConCap (the amount revised downward

after ConCap developed earnings problems), including $74.95 mil. cash and $27.5 mil. preferred stock. The preferred bears no dividend in 1986 and dividends in 1987 and 1988 are contingent upon ConCap earnings. After that the preferred receives $8/sh. ($4 mil. annually). Depending on ConCap future earnings, JAC may also have to issue $25 mil. subordinated notes and $90 mil. additional consideration to ConCap employees and former owners.

Exposure - B: JAC has developed a computerized system that lets it manage widespread properties easily, thus giving it an edge in seeking to consolidate this highly fragmented business. By acquiring Calif.-based ConCap, it ends risk that an independent ConCap would give management of its properties to another company. But ConCap also puts JAC into the ranks of major realty syndicators, where sales of new programs and profits are often determined by tax law changes and investment trends. Recent ConCap syndication sales have been recovering and JAC sees about $300 mil. new equity sales in 1986, about level with 1985. Also ConCap has $200 mil. for mortgage lending and property acquisitions, which would generate new fees. JAC has an innovative, aggressive record and should do well in planning to meet change. Part of its success will depend upon what happens to ConCap's four managed REITs, reviewed briefly below.

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Consolidated Capital Realty Investors falls to C Rank in our review, even tho we do not yet have final numbers on its Nov. 1985 fiscal year. CCPLS trades at $12.50 on NASDAQ. It traded as high as $18.50 during the last 12 months and fell about 26% during 1985. CCPLS was organized in 1975 as ConCap's early version of a "vulture" fund, formed to acquire semi-distressed properties of that day.

EPS/Dividends - C: CCPLS earned 34¢ from operations in the 9 mon. thru Aug., down 48%. In addition it netted $1.40/sh. from property and note sales, bringing total income to $1.74/sh., up 100%. The changing income mix jibes with CCPLS' transition from an operating REIT to one moving toward liquidation. Dividends have held level at $1.68 during this transition, so shares yield over 13%. About 93% of 1985 payout likely will be treated as capital gain; this mix may also hold in future years.

Property sales: CCPLS continues to sell properties and in Oct. sold two Houston apartments with 572 DU. The properties had been operating with negative cash flow and the deal terms illustrate how difficult selling has become in Houston: CCPLS received $34,000 cash on an $8.3 mil. sale ($14,500 per DU) with the rest coming from a $4.2 mil. subordinated note at 8% and $4.1 mil. first mortgage. It also received an option for sale of its 448-DU Polynesia Village apartments in Tacoma, Wash. If that sale closes, CCPLS will be left with 12 properties, including nine in Houston and one each in Wash., Utah and Idaho. Adjusted for the Oct. sales, CCPLS holds $73.2 mil. in cost-basis of properties subject to $40.5 mil. mortgages. CCPLS expects to operate these properties at a negative cash flow including capital improvements, and sell up to five properties yearly to maintain REIT qualification. The Houston concentration could lengthen disposition.

Notes receivable sales: Since CCPLS frequently sells properties by taking back wrap-around mortgages, it has built a $91.6 mil. portfolio of notes and contracts receivable. After $27.2 mil. related payables, CCPLS has $64.4 mil. net equity in these notes. How liquid are they? In Aug. CCPLS sold two notes for $10.5 mil. cash, reporting a $269,000 gain for book purposes and $1.7 mil. taxloss; CCPLS' net equity was discounted 10.6% in the deal. But at end of Aug. CCPLS was pursuing foreclosure on four (of 25) previously sold apartments, including three against one owner who has declared bankruptcy. In similar situations, CCPLS has frequently resold properties at a profit.

Financial Measures - C: Direct debt of $47.6 mil. at Aug. ($3 mil. short-term notes plus mortgages) is 1.2 times $39.7 mil. net equity. Net equity plus depreciation equals $11.48/sh. Liquidity is tight.

Exposure - C: With properties clustered in Houston, CCPLS is a recovery candidate. Management historically has been agile in tough markets.

Consolidated Capital Income Trust (CCITS--$15.88) and **Consolidated Capital Special Trust** (CCSTS--$13.63) are Con-Cap's two mortgage lending trusts which experienced serious problem loans last summer. Both fell sharply in price last year: Income down 41.0% for the year, Special down 50.4% to rank No. 3 and 2 respectively among biggest losers. Both were aggressive lenders, lending to borrowers who had an immediate need to close a transaction. Both sought premium yields of 5%-6% or more over prime in belief that managers could handle expected problems promptly and any losses would still leave them with above-average yields.

Both are now changing to finite life trusts, expected to be liquidated in about 10 years. Both are being redirected into mainstream lending (they have about $200 mil. available) under leadership of a new banking executive who's agreed to come on board in Feb. Here's a statistical look at the two:

	Income	Special
Total assets (Mil.$)	$ 433	$ 300
Non-earning asset-%	32.3%	20.2%
Book value/share	$20.34	$18.26
Recent price	$15.88	$13.63
Dividend rate	$ 2.40	$ 2.16
Yield	15.1%	15.8%

Both stocks have moved up, by 19% and 17% respectively, from last summer's lows. Both are best viewed as low grade bonds, since new management says it expects to be able to hold the indicated dividend rates (which approximate 12%/yr. on net book value, or 1% monthly). Payouts of both over the 10-year liquidation are estimated to be about 70% tax-free return of capital, meaning investors can get an interesting after-tax return even if stock prices don't move up. Credibility of new management is crucial in any such commitment.

SPECIAL REVIEW: WESPAC INVESTORS FALLS AFTER DECIDING TO LIQUIDATE ON ITS OWN

Wespac Investors Trust is another West Coast REIT that was among 1985's biggest losers (off 38.5%) for reasons that have little to do with underlying value, which appears well above recent price (6--OTC). WESPS broke away in Oct. from the Newport Beach, Cal. syndicator that sponsored it, hired separate management, and hopes to sell all properties within two years of its April 1985 liquidation vote. But some widely publicized problems in two other REITS (Wespac II and III) sponsored by the original backer have spilled over into the market (guilt by association). Confusion over a switch from monthly to quarterly dividends (at 72¢ annual rate, down 33% from the previous $1.08 rate) and suspension of dividend reinvestment plan also hurt.

EPS/Dividends: WESPS lost 86¢ sh. from operations in its Aug. 1985 FY but reported 95¢ gain on property sales, for 9¢ sh. net income. Gross cash flow was 87¢ before mortgage amortization. Rental income fell and interest income rose as WESPS sold 6 properties in the year. Property sales included four apartment projects with 714 DU sold for $18.1 mil. ($25,400/DU average); and one shopping center and one office sold for $3.8 mil. All were in Mo., Kan. and Ill. WESPS received $2.9 mil. cash (13.4%) and took back $18.96 mil. notes wrapping around $10.4 mil. underlying first mortgages. WESPS in addition borrowed $5.4 mil. secured by its $8.6 mil. net equity in these notes.

Financial Measures: Mortgage debt of $61.1 mil. is 1.75 times the $35 mil. total net equity plus accumulated depreciation ($5.87/sh.). WESPS owns $95.8 mil. cost basis properties plus $16.5 mil. discounted value of notes receivable. Properties remaining are five apartments with 1,640 DU; 13 shopping centers with 1.03 mil. sq. ft.; and four offices with 209,000 SF. Locations are widely dispersed.

Current value: Appraisals in Aug. 1984, made in conjunction with the liquidation proposal, indicated net values of $83.9 mil. or about $14/sh. In 1983 the trust rejected merger with Southmark for $14/sh., all in SM paper. Allowing for some value slippage, sales expenses, and haircuts on purchase money notes (WESPS sold some seasoned notes last Aug. at a 7% discount), we feel comfortable with $11.50-$12/sh. value.

Outlook: WESPS has sold only one small property since Aug. but is discussing bulk sale to an institution, whose closing is of course not certain.